

IN THE HIGH COURT OF GUJARAT AT AHMEDABAD

INCOME TAX REFERENCE No 281 of 1983

For Approval and Signature:

Hon'ble MR.JUSTICE R.K.ABICHANDANI and
MR.JUSTICE KUNDAN SINGH

- =====
1. Whether Reporters of Local Papers may be allowed to see the judgements?
 2. To be referred to the Reporter or not?
 3. Whether Their Lordships wish to see the fair copy of the judgement?
 4. Whether this case involves a substantial question of law as to the interpretation of the Constitution of India, 1950 of any Order made thereunder?
 5. Whether it is to be circulated to the Civil Judge?

JYOTI ELECTRIC MOTORS LTD

Versus

COMMISSIONER OF INCOME TAX

Appearance:

MR HM TALATI for Petitioner - ABSENT

MR B.B. NAYAK with MR MANISH R BHATT for Respondent No. 1

CORAM : MR.JUSTICE R.K.ABICHANDANI and
MR.JUSTICE KUNDAN SINGH

Date of decision: 17/04/98

ORAL JUDGEMENT (Per R.K.Abichandani,J.)

The Income Tax Appellate Tribunal, Ahmedabad has referred the following question for the opinion of this Court under Section 256(1) of the Income Tax Act, 1961:-

"Whether, on the facts and in the circumstances

of the case, the Tribunal was right in holding that the Commissioner was justified in passing the order under Section 263 of the Act in setting aside the assessment order."

2. The matter relates to the Assessment Year 1976-77, in which the question cropped up as to whether the assessee company which was doing the business of manufacturing and selling electric motors, was entitled to deduct a sum of Rs. 3,25,927/- as payment of royalty made to the licensor Jyoti Limited for providing it with technical knowhow in the form of drawings, designs, technical documents etc., as revenue expenditure. The ITO allowed the claim. However, the CIT noted that the advantage derived by the assessee company in consideration of the payment of the said amount was of an enduring nature, which would endure even after the license agreement was over. It therefore appeared to him that the payment of the said amount was of capital nature and therefore, not admissible as a deduction in computing the income from business. The Commissioner therefore, issued a show cause notice under Section 263 of the Act on the ground that the order passed by the ITO on this point was erroneous and prejudicial to the interest of the Revenue. The assessee was heard in response to the notice and it contended that the royalty paid was only a licence fee. The assessee relied upon a decision of this Court in CIT Vs. Jyoti Limited, reported in 118 ITR 499 in support of its contention that the expenditure should be treated as revenue expenditure. The Commissioner held that the duration of agreement was from 1st September, 1972 upto 10th March, 1972 which stood extended until terminated by either party. It was therefore held that the advantage derived by the assessee was of an enduring nature. The Commissioner held that the assessment order was erroneous and prejudicial to the interest of the Revenue and set-aside the same with a direction to the ITO to examine the terms of the agreement and decide the matter afresh. The Tribunal in appeal filed by the assessee held that the expenditure in question was prima-facie expenditure of capital nature as held by the Commissioner and therefore, the Commissioner was justified in exercising his jurisdiction under Section 263 of the Act. The Tribunal made it clear that the ITO after examining the agreement and other material, would be justified in passing any order which he thinks proper on merits.

3. The assessee's case is that the assessment order was neither erroneous nor prejudicial to the interest of the Revenue and that order of the ITO was in conformity

with the provisions of law and in accordance with the decision of this Court in Jyoti Limited (supra) and therefore, there was no valid ground for the Commissioner to exercise his powers under Section 263 of the Act.

4. It will be noted from Article 4 of the Licensing Agreement that for the supply of additional design and manufacturing drawings and other information, necessary to disclose any modification and improvements made in the products, the licensor was to be paid by the assessee licensee one half per cent royalty in addition to the royalty mentioned in Article 8 of the agreement. As provided by Article 4A, one set of initial drawings and technical documentation was to be supplied to the licensee free of charge. The duration of agreement as provided under Article 2 was from 1st September, 1972 upto 10th March, 1982 and even after the expiry of agreement, it was to continue in force until terminated by giving one year's notice in writing. It would therefore, prima-facie appear that the assessee had acquired a benefit of enduring nature. As held by Hon'ble the Supreme Court in Jonas Woodhead & Sons (India) Limited V. CIT, reported in 224 ITR 342, the sum paid for a benefit of enduring nature such as for obtaining technical knowhow, the drawings, specifications, blueprints of production and testing equipments etc. would constitute capital expenditure. The Tribunal rightly distinguished the decision of this Court in CIT Vs. Jyoti Limited (supra) because in that case, on the basis of the terms of the collaboration agreement, it was found that the property in the specifications, drawings etc. did not pass to the Indian manufacturer and there was no question of acquisition of assets of a capital nature by the assessee so far as these drawings, designs, patterns etc. were concerned.

The Commissioner, under Section 263 of the Act, is empowered to make an order enhancing or modifying the assessment, or cancelling the assessment and directing a fresh assessment, if he considers that any order passed by the Assessing Officer is erroneous in so far as it is prejudicial to the interest of the Revenue. The Commissioner had lawfully exercised his powers under Section 263 of the Act and taken a decision after giving the assessee an opportunity of being heard in the matter, as envisaged by that provision. The Tribunal was therefore, right in holding that the Commissioner was justified in passing the order under Section 263 of the Act setting aside the assessment order and directing the ITO to take a fresh decision.

The question referred to us is therefore,
answered in the affirmative against the assessee and in
favour of the Revenue. The reference stands disposed of
accordingly with no order as to costs.

*/Mohandas